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Supreme Court of the United States

October Term, 1935

No. 270

THE PRUDENCE COMPANY, INC.

Petitioner

v.

FIDELITY AND DEPOSIT COMPANY OF MARYLAND and AMERICAN BONDING COMPANY OF BALTIMORE

BRIEF OF PETITIONER

ALFRED T. DAVISON
Counsel for Petitioner

ALFRED T. DAVISON
MARTIN A. SCHENCK
ORRIN G. JUDD
Of Counsel

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Argued by
ALFRED T. DAVISON

Supreme Court of the United States

October Term, 1935

No. 270

THE PRUDENCE COMPANY, INC.,
Petitioner,

v.

FIDELITY AND DEPOSIT COMPANY OF MARYLAND and AMERICAN BONDING COMPANY OF BALTIMORE.

BRIEF OF PETITIONER

This case is before this Court on certiorari, limited to the measure of damages, granted October 14, 1935 (R. p. 886) to review the decree (R. p. 885) of the United States Circuit Court of Appeals, Second Circuit, made June 17, 1935, which decree reversed the judgment (R. p. 61) of the United States District Court for the Southern District of New York entered June 14, 1934, for $781,694.56, in favor of petitioner as plaintiff, against the respondents as defendants, and which decree also ordered a new trial.

Opinions Below

The opinion of the District Court (R. p. 498) is reported in 7 F. Supp. 392.

The opinion of the Circuit Court of Appeals (R. p. 877) is reported in 77 F. (2d) 834.

The Action

This is an action at law by petitioner to recover from respondents damages due petitioner as obligee under the guaranty (of completion) and indemnity bond for $3,000,000 given by respondents in order to induce petitioner to advance as a building loan the sum of $6,650,000* to Central Park Properties, Inc., for the construction of, and to be secured by mortgage on, the apartment hotel known as Essex House, which is the largest apartment hotel in New York (R. p. 225).

Petitioner was the plaintiff in the District Court and is hereinafter sometimes referred to as "Prudence Company." Respondents are sometimes hereinafter referred to as "Sureties." Central Park Properties, Inc., is sometimes hereinafter referred to as "Principal."

Unless otherwise indicated, the italics in this brief are added by the authors.

The Issue

The certiorari is limited to and the question brought up for review is, the measure of damages to which petitioner is entitled as obligee under such surety bond upon its breach.

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* The entire $6,650,000 was advanced by Prudence Company, and $75,000 was repaid (R. p. 112).

The issue in this Court is mainly whether Prudence Company's damages on such breach of said surety bond should include interest lost by it on the unpaid $6,575,000 building loan (so made in reliance on such bond), between the date specified in the bond for completion of the building by the Principal and the date of its actual completion by Prudence Company, and should also include taxes and insurance premiums which Prudence Company paid during the period of completion.

Statement of the Case

The Surety Bond

Said surety bond (with respect to the issue now before this Court):

1. Guaranteed the construction and completion *not later than December 16, 1930* of the modern 40-story and basement fireproof hotel, specifically described and identified (R. p. 595) in strict accordance with the building loan agreement and with the plans and specifications therein referred to, so as to be *ready for occupancy as a modern hotel, with all equipment installed* (furniture only excluded) not later than December 16, 1930.

2. Obligated respondents as Sureties to "*fully indemnify*" Prudence Company "against any and all loss or damage by reason of failure of the Principal to • • • complete said building • • • *within the time aforesaid*" and in accordance with the plans and specifications (R. p. 596).

3. Obligated such Sureties "to make good any and every default on the part of the Principal" in performing any of the terms, covenants and conditions which the Principal had agreed to keep and perform in the building loan agreement *up to and including the completion* of and payment for said building (R. p. 596).

4. Provided that upon default by principal and/or Sureties, Prudence Company might

(1) complete in general accordance with the building loan agreement and plans and specifications (R. p. 602); and

(2) "do all other acts and things deemed necessary or proper by the Obligee" (Prudence Company) "to complete and equip said building" (R. p. 602),

and also

5. Provided that the sureties should repay Prudence Company "any and all sums of money paid by the Obligee" (Prudence Company) "for the purposes" just enumerated "with interest" (R. p. 602).

The size of the surety bond ($3,000,000) indicates that the parties contemplated and envisaged very serious and large losses to Prudence Company in case the conditions of the bond were not fully complied with.

The Building Loan

Prudence Company was an investment corporation under the Banking Law of New York, engaged in making building loans (on as many as 120 buildings at a time—R. p. 130—).

Respondents are paid sureties.

The Sureties' Principal (Central Park Properties, Inc.) wanted a mortgage loan on this apartment hotel *to be* erected, and desired advances of that mortgage loan before completion—a building loan.

The detailed plans and detailed specifications of what such building was to be were prepared, submitted to Prudence Company, modified to meet its requirements, approved and identified (R. pp. 67-68, 157).

The documents binding the relation of the parties are:

1. the building loan agreement (Exh. 1) between the Principal (Central Park Properties, Inc.) as borrower, and Prudence Company as lender (R. p. 567);

2. the surety bond (Exh. 2) on which this action is predicated, which expressly incorporated the building loan agreement as part thereof (R. pp. 592-93).

In addition to obligating the Principal to erect the building within the time specified, the building loan agreement also obligated the Principal to execute and deliver to Prudence Company a bond and mortgage and provided for many of the terms of such bond and mortgage, and also (R. p. 568) obligated the Principal:

> "to perform and comply with all and every of the covenants, terms and conditions herein *and in said bond and mortgage contained.*"

Prudence Company was also furnished with the personal guaranty of A. E. Lefcourt, President of the Principal, Central Park Properties, Inc., guaranteeing completion of the building and punctual payment of full principal and interest of the bond and mortgage (but not promising indemnity). It is to be noted, however, that this bond by its terms expired and became null and void on the issuance of a certificate of occupancy (R. p. 681). The certificate of occupancy was issued October 3, 1930 (R. p. 879), "but this was not a certificate of completion" (R. pp. 494, 879); and the building had not then been completed, nor the full amount of the building loan advanced.

The full amount of the building loan was advanced and there is now no dispute that all such advances were made in pursuance of the building loan agreement.

$75,000 was paid on account of the loan, leaving as the total unpaid amount of the mortgage loan advanced $6,575,000 (R. p. 112).

Respondents sought to ground a defense on the nature of this payment of $75,000, but the District Court and the Circuit Court of Appeals definitely found against the respondents, both on the law and facts with respect to this defense (R. pp. 514, 879-80).

Defaults

Defaults under the surety bond (and this includes the building loan agreement) are conceded.

Concededly,

1. the building was not completed and ready for occupancy on December 16, 1930;*

2. the building was not constructed in accordance with the plans and specifications and the building loan agreement;†

3. Large amounts of money remained to be expended to bring the building up to the mark of the contract.

The word "concededly" is used advisedly. We need refer only to the verified answers (R. pp. 39, 50, 51) marked in evidence at the trial (R. pp. 249-250) and to the statement of defendants' counsel upon the trial (R. p. 334). In subdivision marked "Twelfth" of the verified amended answer, respondents themselves allege (R. p. 50):

> "TWELFTH: That on the 5th day of December, 1930, the building was in such condition that it would have required a sum in excess of $170,000 to complete the same and make it ready for occupancy, and there were omissions of labor and materials from and substitutions of inferior materials in said building amounting in value to a sum in excess of $230,000."

This is a repetition *verbatim* of subdivision marked "Fourteenth" in the original verified answer (R. p. 39).

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* The date of actual completion was October 1, 1931 (R. p. 111).

† The record shows that after Prudence Company had accepted the loan and made its first advance of $3,250,000 the plans and specifications were secretly, deliberately, intentionally and materially changed (R. pp. 192, 345), and the specifications rewritten by the Principal (R. pp. 371-373). Many items were omitted and many substitutions of inferior materials made, in respects which the proof shows detracted from the appearance, value and efficient operation of the building (R. pp. 161, 182, 220, 434-35, 471-72, 482-83).

For a third repetition of the concession and admission, see subdivision marked "Twentieth" of the amended answer of both defendants (R. p. 51).

The District Court's findings of fact with respect to such defaults were not questioned by the Circuit Court of Appeals.

Completion by Prudence Company

Prudence Company completed the building after notices to the respondents giving opportunity to them to complete (R. pp. 730, 738) and after their failure to do so. During the course of such completion Prudence Company expended large sums of money for labor and materials and also for taxes and insurance premiums on this building.

Prudence Company, in accordance with its rights under the bond (R. pp. 602-603), did not, in certain instances, go to the expense of remedying substantial departures from the plans and specifications, but proved the cost of supplying the items omitted, and also proved the difference in value between the inferior materials substituted and the materials called for by the plans and specifications.

Foreclosure and Deficiency Judgment

Before completing the building Prudence Company caused its mortgage to be foreclosed in the name of its representative and nominee, James T. Harrigan, and on the foreclosure sale the property was bought in by said James T. Harrigan, who "represented and was the nominee of" Prudence Company. In such foreclosure action

a deficiency judgment was entered April 30, 1931 for $716,215.02,* no part of which has been collected.

The amount of such deficiency judgment with interest from April 30, 1931 is more than the amount of the judgment obtained by Prudence Company in this case.

Defenses

All the defenses set up by the Sureties (and there were ten separate defenses originally) were either stricken out by the District Court on motions before trial (see orders and opinion of Judge Bondy, R. pp. 523, 536, 541—2 F. Supp. 454—) or were held not proved at the trial (see opinion of trial Court—Judge Galston—R. p. 498); and the Circuit Court of Appeals was in accord with such dispositions thereof except only with respect to one aspect of the partial defense of oral waiver, fully discussed in the briefs on the application for certiorari, and mentioned later in this brief (pp. 13-14n., 56).

The Trial, Verdict and Judgment Thereon

The case was tried, pursuant to written stipulation (R. p. 65), before a jury of one, and it was agreed that both parties should be deemed to have moved at the conclusion of the trial for a directed verdict without reservation of any right to have any issue or issues submitted to the jury.

Petitioner proved three items of damage, viz.:

(1) actual payments made in completing the building, including taxes and insurance premiums paid by petitioner during the period of completion;

* All the facts with reference to the foreclosure by James T. Harrigan, as representative of and nominee of Prudence Company are set forth in subdivision marked "XXXIX" of the complaint (R. pp. 19-20), which was offered in evidence by the respondents on the trial (R. p. 314).

(2) estimated cost of supplying omissions, and difference in value by reason of inferior substitutions,

and

(3) interest which petitioner lost on its capital investment between the time the building should have been completed and the time it was actually completed.*

Pursuant to the stipulation the trial Court, after the trial, directed a verdict in favor of Prudence Company for $777,934.54 (R. pp. 63, 515) which, with interest from the date of the verdict to the date of the entry of judgment, made up the amount of the judgment entered June 14, 1934, namely $781,694.56 (R. pp. 61-62).

Such judgment includes three types of damages to Prudence Company (R. pp. 515, 516, 63):

I. Amount expended by Prudence Company in the completion of the building (including insurance premiums in the sum of $1,640.87 and taxes in the sum of $57,120)	$209,454.85	
Interest thereon to May 15, 1934	33,765.93	$243,220.78

* In addition to proving that the cost of completion was reasonable (R. p. 233 and Exhibit 84, R. p. 758) petitioner proved that the time taken for completion was reasonable. Not only does reasonable cost of completion necessarily include the fact that the time required for completion was entirely reasonable, but also, inasmuch as the payrolls included in the cost of completion (Exhibit 84, R. p. 761) necessarily involved the question of time, the testimony offered by petitioner that such

II. Amount representing estimated cost of supplying omissions of materials called for by plans and specifications	$143,842.28	
Interest thereon from December 16, 1930, to May 15, 1934	29,426.76	$173,269.04
III. Amount of interest lost by Prudence Company by reason of failure to complete on or before December 16, 1930, being interest on $6,575,000—net amount advanced on building loan mortgage—from December 16, 1930, to date of completion, October 1, 1931 (as alleged in subdivision XXXVII (3) of the complaint)	312,357.53	
Interest thereon from October 1, 1931, to May 15, 1934	49,087.19	361,444.72
Total amount of verdict		$777,934.54

payrolls were necessary and reasonable, establishes that the time taken was reasonable.

This appears, moreover, from the fact that Mr. Lukach, who was in charge of completion for Prudence Company, was at the building every day and all of every day until October 1, 1931, the date of completion by petitioner (R. p. 237).

While it was not incumbent upon petitioner to perform the obligation of the bond which the respondents had breached—since completion was an obligation of the sureties—we mention these facts because the sureties have previously based an argument on the contention that there was no evidence of what constituted a reasonable time for completion.

Interest thereon from May 15, 1934 (date of direction of verdict) to June 14, 1934 (date of entry of judgment on the verdict)	3,760.02
Total amount of judgment	$781,694.86

The Decision of the Circuit Court of Appeals

The grounds upon which the Circuit Court of Appeals reversed are:

1. that the measure of damages on the breach of this guaranty of completion and indemnity does not permit recovery of

(a) the interest which Prudence Company lost on the money it had actually advanced on the mortgage loan on the building (which was not completed) between the date it should have been completed (December 16, 1930) and the date of the actual completion by Prudence Company (October 1, 1931); or

(b) taxes ($57,120) and insurance premiums ($1,640.87) which Prudence Company was required to pay for the period between the date the building should have been completed and the date it was completed; and

2. the exclusion of evidence described by that Court as "tending to show," if proper foundation had been laid, a parol waiver or release of requirements of the building loan agreement and plans and specifications.

But for the one aspect of the partial defense of waiver with respect to which the Circuit Court of Appeals stated there was evidence "tending to show" parol waiver, judgment could be directed for the amount of damages to which Prudence Company is entitled.*

Thus the rule of damages which the Circuit Court of Appeals has laid down is limited to

> (1) cost of labor and materials required for completion, and
>
> (2) loss due to omissions and items of inferior substitution,

the opinion stating (R. p. 884):

> "Upon a new trial, which must be had, in establishing appellee's damages, the rule of cost of completion will be the guide. Evidence of experts as to the difference in value showing cost of completion, evidence of actual cost, and experts' testimony as to cost of completion, may be received.

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* While this certiorari is limited to the measure of damages, no statement of the case would be complete without calling attention to the fact in this connection:

> (1) that the bond provided that *any waiver or release* by Prudence Company of any default or omission by Principal and/or Surety in complying with the building loan agreement or plans and specifications *must, in order to be binding upon Prudence Company, be* (1) *in writing,* (2) *signed by duly authorized officers of Prudence Company, and* (3) *specify* "the item or items specifically so released" (R. p. 604);
>
> (2) that the provision just quoted was contained *not* in the building loan agreement but in the bond, and there is no claim that the parties *to the bond* ever varied its provisions;
>
> (3) that the only evidence which the Circuit Court of Appeals referred to as "tending to show" parol waiver

> "Loss due to items of inferior substitution unless effectively consented to by the appellee may also be recovered."

The Circuit Court of Appeals also stated (R. p. 881):

> "The true measure of damages to this appellee, is the extent to which its security was impaired by the failure to complete in accordance with the plans and specifications."

Clearly, as we interpret such a statement, the loss of interest during the time necessary to complete, together with the taxes and insurance premiums which must be paid, constitute part of the measure of impairment of the security which a completed building was intended to afford.

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was a vague question (R. p. 213) put to a former architect of the Principal, on cross examination (having no relation to the witness' *direct* testimony, and excluded, among other reasons, as being improper cross examination), with respect to a conversation had at a time when he represented none of the parties to the litigation,

(4) that the Circuit Court of Appeals held the exclusion of such evidence was prejudicial error only *"if"* Prudence Company's "president had authority to waive the requirement of written waiver and consent" (R. p. 883); but that there was no proof that the Prudence Company's President had such authority; and, on the contrary, the proof was that all changes were actually passed upon by a committee (R. pp. 134, 136) of which the President was not a member;

and

(5) that *neither the evidence excluded nor any evidence offered at the trial purported to relate to the waiver of any specific item of the plans and specifications.*

Specifications of Error Intended to Be Urged

The Circuit Court of Appeals erred:

1. In holding that none of the items of interest, taxes and insurance, for the period between the date fixed for completion of the building and the date of actual completion, was recoverable under the applicable rule of measure of damages.

2. In holding that interest lost on the loan, and taxes and insurance paid, for the period between the date fixed for completion of the building and the date of actual completion, were not within the contemplation of the parties at the time of the execution and delivery of the surety bond.

3. In holding that there is no evidence to support the finding of fact by the trial Court that interest, taxes and insurance were each within the contemplation of the parties.

4. In holding that, in the absence of express contract to pay the interest lost on the mortgage loan, interest as damages, even though within the contemplation of the parties, cannot be recovered under the surety bond, and that there was no evidence to support the District Court's finding on this point.

5. In holding that there is no condition, express or implied, in the surety bond, respecting payment of interest on the loan, taxes or insurance, and that no liability exists therefor, and that none of them are within the undertaking of the surety companies.

6. In holding that, under the decision of the Court of Appeals of the State of New York in *Kidd* v. *McCormick*, 83 N. Y. 391, and the decision of this Court in *Trainor Co.* v. *Aetna Casualty Co.*, 290 U. S. 47, interest, taxes and insurance are not recoverable as damages on the breach of the surety bond.

7. In holding that the true measure of damages to the Prudence Company is the extent to which its security was impaired by the failure to complete the building in accordance with the plans and specifications.

8. In holding that any court can pass upon the margin or nature of security to which the Prudence Company is entitled under the building loan agreement and surety bond in this case.

9. In holding that the Prudence Company was not entitled on December 16, 1930, to a completed building, which could be immediately rented and availed of as a source of income, out of which to pay interest, taxes and insurance.

10. In holding that the Prudence Company cannot recover interest as damages by reason of the failure to complete said building on December 16, 1930, in the absence of proof showing loss of rent during the period of incompletion.

11. In holding that the parties did not contemplate at the time of the building loan agreement that the building would rent and was capable of being rented for more than enough to pay interest, taxes and carrying charges.

12. In holding that interest, taxes and insurance should not be included as damages under a rule of measure of damages based upon the difference between the value of the building on December 16, 1930, as the work had progressed, and the value it would have had on that day, if completed strictly in accordance with the plans and specifications.

Argument

Outline of Points to Be Argued

Foreword.

POINT I.—Interest, taxes and insurance premiums as items of loss and damage to petitioner are recoverable as part of the damages within the contemplation of the parties.

1. **The applicable decisions of this Court and of the New York Court of Appeals justify and require the allowance of interest, taxes and insurance as part of the damages caused by the failure to complete the building at the time guaranteed.**
2. **The facts and circumstances under which this surety bond was given, as well as the provisions therein contained, specifically show that interest, taxes and insurance premiums were within the contemplation of the parties as items of damage in case of breach.**
3. **On the principle that interest bears the same relation to money as rent does to land, interest is clearly recoverable as an item of damage.**
4. **The trial Court found as a fact that interest, taxes and insurance were within the contemplation of the parties.**

5. Interest is recognized as part of the measure of damages for breach of contract, where loss of such interest was within the contemplation of the parties.

POINT II.—In addition to being within the contemplation of the parties, interest, taxes and insurance premiums are recoverable because necessarily included in the general rules of damages applicable to bonds guaranteeing completion.

POINT III.—The provisions of the surety bond in this case specifically obligated the surety in express terms to pay interest on the loan, and taxes and insurance on the mortgaged property, until the date of actual completion of the building in accordance with the plans and specifications.

1. As to interest.
2. As to insurance.
3. As to taxes.

POINT IV.—The measure of damages adopted by the trial Court was supported by proper evidence, and conformed with all legal requirements.

CONCLUSION.—Both sides having moved for the direction of a verdict, there is no restriction on the power of this Court to direct such judgment as the Circuit Court of Appeals should have directed: viz., either (1) affirming the judgment of the District Court, because the exclusion of so-called evidence "tending to show" parol waiver was not such of itself as to require a new trial, or (2) if a new trial is to be had, directing that the issue on such new trial be limited to the question of the effectiveness of any alleged waiver of omissions or substitutions.

Foreword

From whatever angle the facts in this case are considered, Prudence Company's capital investment is the central feature.

The protection of such capital investment was the motivating cause of the surety bond.

Prudence Company required security and the parties agreed that such security would be a specific building, completed and ready for occupancy, with all equipment installed, not later than a fixed and certain date—December 16, 1930.

Obviously, there would not be adequate security until the building was completed and ready for occupancy.

Until that time, this surety bond for $3,000,000 filled the gap and was the basis on which Prudence Company not only agreed to, but did actually, make the advances of $6,650,000.

POINT I

Interest, taxes and insurance premiums as items of loss and damage to petitioner are recoverable as part of the damages within the contemplation of the parties.

Ever since *Hadley* v. *Baxendale*, 9 Exch. 341, 354, 356 (1854), the law has been well settled and unquestioned that damages on a breach of contract

> "should be * * * such as may reasonably be supposed to have been in the contemplation of both parties, at the time they made the contract, as the probable result of the breach of it."

Hadley v. *Baxendale* (*supra*) was expressly approved in *Howard* v. *Stillwell & Bierce Mfg. Co.*, 139 U. S. 199, 207, and *Booth* v. *Spuyten Duyvil Rolling Mill Co.*, 60 N. Y. 487, 492.

Not only the decisions with respect to surety bonds, but an independent consideration of the nature and purposes of a surety bond given to a mortgagee—and particularly of the bond here involved—show that the damages allowed by the trial Court (including interest lost and taxes and insurance premiums paid by petitioner), fall within the reasonable contemplation of the parties, and are justified by the rule of *Hadley* v. *Baxendale*.

1

The applicable decisions of this Court and of the New York Court of Appeals justify and require the allowance of interest, taxes and insurance as part of the damages caused by the failure to complete the building at the time guaranteed.

Clearly, as we submit, this Court has ruled in *Trainor Co.* v. *Aetna Casualty Co.*, 290 U. S. 47, that interest, taxes and insurance are within the damages contemplated by parties to such a surety bond as is the subject of this action. In that case, there was a completion bond given by the Aetna Casualty Co. to Trainor, the mortgagee, which guaranteed that a building and certain improvements would be erected in accordance with plans and specifications upon each of 52 lots upon which Trainor had his mortgage, within ten months from the date thereof.

The trial Court found that on the date fixed for the completion of the buildings and improvements, 28 houses

had not been fully completed, but held that Trainor was entitled to merely nominal damages against the surety, because of the further finding that, although a mortgage prior to Trainor's had since been foreclosed, the value of the property with the uncompleted buildings at the time of default exceeded the sum of his mortgage and all prior liens.

On appeal from the affirmance by the Circuit Court of Appeals, this Court reversed and unanimously held (Mr. Justice SUTHERLAND, p. 55):

> "It is no answer to say that the value of the property immediately after the default exceeded the sum of the mortgage together with all prior liens. Petitioner was then without remedy against the property because its mortgage was not in default. It was, therefore, obliged to sit by and await the action of others over which it had no control. In the meantime, *the uncompleted buildings necessarily lay unrented, subject to expense in the way of taxes, insurance, accumulating interest, etc.*, deteriorating in quality and steadily declining in value. Petitioner is entitled to be put in as good position *in respect of its debt* as it would have occupied if the buildings had been completed in accordance with the terms of the undertaking; and this can be done here only by giving it the amount of the difference between the value of the unfinished buildings and their value as it would have been if completed in accordance with the agreement—see Kidd *v.* McCormick, supra, p. 398—but exceeding neither the amount due on its debt nor the amount of the bond."

Kidd v. *McCormick*, 83 N. Y. 391 (cited with approval in (*Trainor* v. *Aetna*), also clearly recognizes that the dam-

ages which a mortgagee suffers by reason of failure to complete a building on the date called for, include the loss of interest on his own investment during the period of completion, and the taxes and insurance premiums which must be paid—and in this case *were* paid by Prudence Company—during that period, the default in completion having made it impossible to produce any income from the mortgaged property to keep down such carrying charges. In the *Kidd* case, plaintiff conveyed certain property to the defendants, taking back purchase money mortgages which be subordinated to new first mortgages. Defendants undertook to erect houses on each of the lots, and plaintiff agreed to aid by temporary loans. In order to induce the plaintiff to so subordinate and to make such loans, it was agreed that a special fund should be provided out of the proceeds of the first mortgages, to be paid to plaintiff when the buildings were completed and ready for occupancy. Defendants defaulted in completing; plaintiff foreclosed, bought in the property, and completed the buildings; and the question was raised concerning the rights of the plaintiff as second mortgagee in such special fund so deposited for the completion of the buildings.

Judgment went for the plaintiff (second mortgagee) in the sum of $2,250 with interest, which the Referee found to be the difference between the value of the uncompleted houses and the value they would have had if finished on the agreed date; the record on appeal therein (fols. 15, 84, 259, 268), and the concessions of the plaintiff himself (Brief in Court of Appeals, p. 6) show that the amount recovered ($2,250) was more than the plaintiff's actual payments for labor and materials used in completing the buildings.

In affirming this judgment, the New York Court of Appeals said (p. 395):

> "• • • Clearly he" (plaintiff, second mortgagee) "is entitled to have from the McCormicks as much as will put him in as good plight as he would have been had the houses been finished."

and at page 398:

> "The plaintiff was entitled on the 1st of September, 1877, that there should be finished houses, *rentable,* and so, *productive of income with which* to keep down *interest on the mortgages on the lots, the taxes thereon, and insurance premiums.* He could not, on that day, had he been let into immediate possession and control, by any expenditure of money or energy, have completed them at once; nor, in the nature of things, could he have supplied the lack of the completed houses by a purchase in the market. *The work needed to complete was one of time; and while the time was running, interest was running also, taxes were levied, insurance was to be kept up, and the premises were yielding no rent. It is plain that to repay him just what he expended to finish the buildings would not make him whole; for he had to* pay, besides the cost of building, interest to Granniss" (first mortgagee) "and *lose interest on his own mortgages, and pay taxes and premiums.*"

In *Kidd* v. *McCormick* there was no surety bond with the many and specific obligations which are in the bond in this case. That case, for that reason, is even stronger authority for the inclusion of interest, taxes and insurance under an express bond of guaranty and indemnity, and indicates what subsequent to that case must have been plain to sureties binding that same relationship.

The above quotation from *Kidd* v. *McCormick* squarely disposes of the argument sought to be made by respondents in the Circuit Court of Appeals and also on the application for certiorari here, to the effect that the *Trainor* and *Kidd* cases are distinguished by the fact that the plaintiffs therein were junior mortgagees. As the Court of Appeals stated in *Kidd* v. *McCormick,* even if the junior mortgagee in that case had been let into immediate possession and control the work needed to complete was one of time, and while the time was running, interest and taxes and insurance premiums were also running. The Court thus held that the junior mortgagee's loss of interest on his own mortgage was part of his damage. It follows, therefore, that the rule of damages, which must be compensatory, is the same whether the obligee be a first mortgagee or a third mortgagee.

For the same reason that this Court and the New York Court of Appeals were unable to think and speak of damages sustained by a mortgagee by reason of the non-completion of a building which had been guaranteed to be erected, except in terms of interest, taxes and insurance premiums as part of such damages, so also the parties to this action must have contemplated, and certainly are to be deemed to have contemplated, that interest, taxes and insurance were part of the damages to be sustained on the breach of the contract in this case.

If interest, taxes and insurance be not included in petitioner's damages, then the rights recognized by this Court in *Trainor Co.* v. *Aetna Casualty Co.,* that

> "Petitioner is entitled to be put in as good position in respect of its debt as it would have occupied if the buildings had been completed in accordance with the terms of the undertaking";

and by the New York Court of Appeals in *Kidd* v. *McCormick*, that

> "he" (plaintiff, second mortgagee) "is entitled to have from the McCormicks as much as will put him in as good plight as he would have been had the houses been finished"

are not fulfilled and petitioner is deprived of a part of the damages actually sustained.

No court has ever questioned the language or the justice of the statement of Chief Judge FOLGER in *Kidd* v. *McCormick*:

> "• • • *It is plain that to repay him just what he expended to finish the buildings would not make him whole,*"

and yet that is just what the Circuit Court of Appeals has done in this case, because it has limited Prudence Company in this case to a recovery of what it expended plus only the expense of bringing the building up to the mark of the contract.

2

The facts and circumstances under which this surety bond was given, as well as the provisions therein contained, specifically show that interest, taxes and insurance premiums were within the contemplation of the parties as items of damage in case of breach.

A

The surety bond guaranteed that the building would be

> "*ready for occupancy* as a modern hotel *not later than the 16th day of December, 1930*, together with

> all equipment customary in a building of the type provided for in said building loan agreement, installed *not later than the said 16th day of December, 1930* • • •'' (R. p. 595)

and the bond is replete with provisions emphasizing the obligation to complete the building *''within the time aforesaid''* (R. pp. 596, 597, 598).

Why the above provision, including "ready for occupancy as a modern hotel not later than the 16th day of December, 1930," "with all equipment • • • installed," if not that the respondents were insuring that from and after December 16, 1930, Prudence Company, upon resorting to the building as security for its loan, would have an immediate source of income with which to pay interest, taxes and insurance, and other carrying charges from and after December 16, 1930?

Buildings are given as security for mortgage investments—and completed buildings are required—in order that in case of default, they may be resorted to as sources of income with which to pay the interest which the borrower has defaulted in paying, and with which to pay the principal when such buildings can be sold.

An uncompleted building is of no use to anyone, and consequently is no security.

Therefore, pending the completion of the building the surety bond was to give Prudence Company the security which the building after completion would furnish—that is, an assurance of a completed structure capable of producing revenue with which to meet not only the interest on the amount advanced, but the carrying charges (including taxes and insurance) on the property which was to be security for the loan.

The difference to Prudence Company between a complete and incomplete building on the date of default was as inevitably the loss of return on its money pending completion as the expense involved in bringing the building to completion. Its money was as idle meanwhile as was the building. And the idleness of the building, within universal contemplation of the parties in such a relationship, was the cause of the idleness of the money.

The above aspect of the relation between the obligation of the parties to this action and the scope of the damages contemplated in case of breach is expressly sanctioned in that part of the opinion in *Kidd* v. *McCormick* which states (p. 398):

> "The plaintiff was entitled on the first of September, 1877, that there should be finished houses, rentable, and so, productive of income with which to keep down interest on the mortgages on the lots, the taxes thereon, and insurance premiums."

B

The surety bond in this case is more than a guarantee of completion. It is also a bond for indemnity.

Among the provisions for indemnity in the surety bond are (R. p. 596):

> "AND IF the said Surety shall fully *indemnify* and save harmless said Obligee," (this petitioner) "its successors and assigns, *from and against any and all loss or damage by reason of failure of the Principal* to construct, fully pay for and complete said building and install, supply and fully pay for such equipment *within the time aforesaid* and as provided for in said building loan agreement and plans and specifications; AND IF said Surety shall

> make good any and every default on the part of the Principal in constructing, paying for and completing said building and supplying, installing and paying for equipment *as aforesaid* * * *."

The Court will note the time element in the provision just quoted.

How can there be indemnity if the petitioner is not placed in just as good a position as if the building had been completed on December 16, 1930, and given the full margin of protection for which it bargained?

How can petitioner's security be preserved unless tax liens accruing against it during the period of completion, and insurance premiums necessary to protect the building during its completion, are paid?

It is impossible to consider the loss of any mortgagee obligee under a bond such as in this case without taking into account the interest lost and the taxes and insurance required to be paid.

If this building had been completed on December 16th, 1930, the petitioner could have immediately resorted to the building as the source of income out of which interest on its mortgage investment could be derived, and taxes and insurance premiums paid.

Petitioner, having lost interest on its mortgage investment from December 16, 1930, until the building was completed, is entitled to look to the defendants for reimbursement for such interest, and for taxes and insurance premiums paid, as items of loss against which defendants indemnified it.

3

On the principle that interest bears the same relation to money as rent does to land, interest is clearly recoverable as an item of damage.

> "* * * In this country interest is the natural growth, or incident, of money, and bears the same relation to it that rent does to land."

Thus spoke Judge O'Brien in *Woerz* v. *Schumacher,* 161 N. Y. 530, 536.

It is well settled that the owner of the land on which a building has been guaranteed to be completed within a certain time, is entitled to the rental value of the land and building during the delay in completion, as a part of the damages flowing directly from the failure to complete the building.

White v. *McLaren,* 151 Mass. 553;
U. S. Fidelity & Guaranty Co. v. *Parsons,* 147 Miss. 335, 53 A. L. R. 88;
Noonan v. *Independence Indemnity Co.,* 328 Mo. 706;
Hexter v. *Knox,* 63 N. Y. 561;
Lord v. *Comstock,* 20 Jones & S. (N. Y.) 548;
Donlan v. *Trust Co.,* 139 No. Car. 212;
Somerby v. *Tappan,* Wright (Ohio) 229, 231; same case on second trial, *id.* 570 (1833);
2 Joyce, Damages, Section 1388;
2 Sedgwick, Damages (9th Ed.) § 645.

There is no escape from the analogy between a mortgagee, whose capital investment is tied up in this land and

building, and the owner of the land and building. In either case failure to complete means a loss—to the owner, a loss of rent, to the mortgagee (who must take over the property), a loss of interest and carrying charges, for which the building, if it had been completed, would have been security—.

It follows that the holder of a *mortgage,* representing a *money interest* in land, is entitled to the interest, corresponding to the rent of an owner, which he loses, during the delay in completion of a building guaranteed to be finished at a specified time.

The Circuit Court of Appeals misconceived the nature of the right to interest, and the relevance of proof of rental value, when it stated:

> "Since the complaint does not plead and no proof has been received showing loss of rent during the period of incompletion, we need not decide whether or not this appellee might have had a loss of profits because of failure to have a completed building after its entry and possession of the premises" (R. p. 884).

Prudence Company, recognizing that the guaranty ran to it as mortgagee rather than as owner, has not asked for the profits which would have resulted from recovery of rents. The defendants have never disputed that rental value would be greater than the interest and carrying charges which Prudence Company was allowed; and to do so would have been inconsistent with their contention (entirely erroneous) that the value of the building in its uncompleted state was sufficient to protect Prudence Company.

The parties obviously contemplated when the building loan agreement and surety bond were executed, that

the building, when erected, would rent for more than enough to pay interest on the mortgage, and taxes, insurance premiums and other carrying charges. Otherwise, (1) Central Properties would never have undertaken to erect the building, (2) the Prudence Company would not have agreed to lend money on its security for its erection, and (3) the holder and guarantor of the prior mortgage on the premises would not have consented to subordinate such mortgage of $1,400,000 to the mortgage being advanced by Prudence Company, or to lend an additional $600,000 on the completed building (R. pp. 584-85). The Principal having been a party to all these three transactions, its Sureties, respondents here, cannot dispute the purposes and objects so obviously in the minds of the parties, and therefore contemplated by them.

Surely, no court can properly assume that the rental value of a modern apartment hotel fronting on Central Park South in New York City would not, in 1931, equal the interest on its first mortgage and taxes and insurance premiums, much less use such assumption as the basis for reversing an item of damage allowed by the trial Court.

4

The trial Court found as a fact that interest, taxes and insurance were within the contemplation of the parties.

The question of what damages were contemplated by the parties at the time the contract was made, is a question of fact. In *Hadley* v. *Baxendale,* 9 Exch. 341, the rule of damages was discussed in terms of the charge to be given to the jury. Other cases likewise treat the question as one for the jury.

Delafield v. *Armsby Co.*, 131 App. Div. 572, 586, aff'd, 199 N. Y. 518;
Holt Mfg. Co. v. *Thornton*, 136 Cal. 232, 68 Pac. 708;
Macleod v. *National Surety Co.*, 133 Minn. 351, 355;
Cf. Sawdon v. *Andrew*, 30 L. T. (n. s.) 23.

The trial Court, in including interest, taxes and insurance in the measure of damages, therefore decided a question of fact as to what damages were contemplated by the parties.

In reversing that finding, the Circuit Court of Appeals violated the well-recognized rule that where both parties have moved for the direction of a verdict, they are concluded by the Court's findings on all issues of fact, and the decision is not open to review if there be any evidence to support it.

Beuttell v. *Magone*, 157 U. S. 154;
Clapper v. *Gamble*, 28 F. (2d) 755, 758 (C. C. A. 8);
American Mercantile Corp. v. *Spielberg*, 262 Fed. 492 (C. C. A. 2);
Williams v. *Vreeland*, 250 U. S. 295, 298.

The documents themselves,—even the size of the surety bond ($3,000,000),—taken with the express provisions of the surety bond guaranteeing the completion of the building "ready for occupancy as a modern hotel not later than the 16th day of December, 1930," and that too "with all equipment installed," as well as the circumstances under which the loan was made by Prudence Company as an investment company under the Banking Law of New York (therefore dependent upon interest), are all facts constituting evidence amply supporting the finding of the trial Court.

5

Interest is recognized as part of the measure of damages for breach of contract, where loss of such interest was within the contemplation of the parties.

There is nothing novel in Prudence Company's claim to interest as a separate item of damage.

A clear example of interest being treated as an independent item of damage is the case of *United States* v. *New York,* 160 U. S. 598, 621, where interest paid by the State of New York on money borrowed to equip troops for the Civil War was allowed as an item of "costs, charges, and expenses properly incurred" for the defense of the United States, although if it were a claim for "interest as such" (p. 624) it could not have been recovered as against the United States. *Cf. Wilbur* v. *United States,* 284 U. S. 231.

The doctrine of *Hadley* v. *Baxendale* has also been applied to allow the recovery of interest on an independent contract. An instance is found in *Meyer* v. *Haven,* 70 App. Div. 529. That case involved a counterclaim by Haven, who had contracted to build shops for a railroad company, for damages caused by Meyer's delay in performing a subcontract for the structural iron work. This delay prevented Haven from completing his own contract with the railroad company on time, and under the terms of that contract delayed his receipt of progress payments, depriving him of the use of $27,800 from December 12, 1892 until June 25, 1893. The Court held that the interest so lost, amounting to $834, was "an item of loss" which "can be traced directly to the plaintiffs' (Meyer's) breach of

the contract" (p. 536), and that, since the terms of the main contract were known to Meyer (and the terms of the building loan agreement in this case were admittedly known to the sureties—R. p. 595), such interest was rightly included in the plaintiff's damages. (See also *Gordon* v. *Curtis Bros.*, 119 Ore. 55, 66.)

In the following additional cases, damages for delay in performing a contract were similarly held to be measured by the interest lost on the sum invested by plaintiff:

Wood v. *Joliet Gaslight Co.*, 111 Fed. 463 (C. C. A. 7);

DeFord v. *Maryland Steel Co.*, 113 Fed. 72 (C. C. A. 4);

American Bridge Co. v. *Camden Interstate Ry. Co.*, 135 Fed. 323, 330-31 (C. C. A. 4);

N. Y. etc. Mining Co. v. *Fraser*, 130 U. S. 611, 622;

See *Sutherland, Damages*, § 703.

In the *Wood* case cited above, the damages were for delay in completing a gas holder, which was required by the plaintiff only during the months of December and January; because it was not completed until the end of January, it was useless and plaintiff's investment in it was idle, until the following December. The Court stated (111 Fed. at 465-66):

> "No evidence was introduced respecting damages, other than that the holder constructed was useless to the defendant-in-error except during the months of December and January; • • • We think the first fact, viz.—that the holder was useless except during the months of December and January—discloses in law a definite measure of damage.

"The amount allowed by the Circuit Court is within a few dollars of a year's interest at five per cent., (the legal rate in Illinois), upon the contract money already paid and the amount invested in the land upon which the holder was erected. * * *

"It seems plain to us that the defendant-in-error was entitled to the loss it suffered by reason of the plaintiffs-in-error's default. In the absence of special damages, such a loss seems correctly measured by the investment tied up on account of the breach. * * * The rule we have adopted is in our opinion sufficiently supported in the case of *Mining Syndicate* v. *Fraser,* 130 U. S. 611, 9 Sup. Ct. 665, 32 L. Ed. 1031."

So, also, in computing damages for breach of an agreement to make a loan, the additional interest paid or payable on the placement of the loan with another lender is an element of damages under the rule of *Hadley* v. *Baxendale,* even though the entire principal of the loan is not a proper measure of recovery. *South African Territories, Ltd.* v. *Wallington,* [1897] 1 Q. B. 692; *Lloyd Investment Co.* v. *Illinois Surety Co.,* 164 Wis. 282, 286, 288.

Perhaps even closer in point is *Macleod* v. *National Surety Company,* 133 Minn. 351. There the suit was by the principal contractor for construction of a school building, on the bond of a sub-contractor, whose delay in furnishing structural ironwork had prevented plaintiff from fulfilling his contract at the agreed time. This delay had caused loss of interest on the final installment of the contract price from the date fixed for completion to the date when the sub-contractor completed his portion of the work. The Court held that the jury were justified in finding that part of the damages "naturally and necessarily resulting from the delay in delivering the material upon the premises" included "interest to the amount of $125 upon an

installment of the contract price to be paid plaintiff on November 1, 1912, the date fixed for the completion of the building and which payment was withheld because of the fact that the building was not completed, such completion being prevented by the default of the Avery Co." (defendant's principal) (133 Minn. at 354).

The above cases show that the Circuit of Appeals was under a misapprehension as to the nature of the right to interest when it stated (R. p. 884):

> "* * * In the absence of express contract to pay the interest, interest as damages cannot be recovered apart from the principal of the debt. *Holden* v. *Trust Co.*, 100 U. S. 72; *Brewster* v. *Wakefield*, 22 How. 118; *Hamilton* v. *Van Rensselaer*, 43 N. Y. 244; *O'Brien* v. *Young*, 95 N. Y. 428."

The cases cited by the Circuit Court of Appeals are cases which apply only the rules (1) that interest after maturity (being awarded as damages and not by virtue of contract) is calculated at the legal rate instead of the contract rate, and (2) that a guaranty of interest up to a certain date cannot be construed as a promise to pay interest beyond that certain date. Rule (1) does not forbid Prudence Company's recovery of interest here, whether as damages or as part of the express obligations of the bond. As for rule (2), it would, if applicable, forbid only interest *after* completion. The surety bond in this case was a bond of guaranty and indemnity "up to and including the completion of" the building (R. pp. 596-97), which was completed on October 1, 1931. No interest beyond that date has been asked or recovered as damages. Nothing in the cases cited by the Circuit Court of Appeals, therefore, prevents the recovery of the interest which was lost as a result of the delay in completing the building.

POINT II

In addition to being within the contemplation of the parties, interest, taxes and insurance premiums are recoverable because necessarily included in the general rules of damages applicable to bonds guaranteeing completion.

Petitioner's recovery of interest lost and taxes and insurance premiums paid is supported not only by the specific decisions discussed in Point I, and the circumstances therein mentioned, showing that such damages were in contemplation of the parties, but is in accord with the specific rules of damages in cases of completion bonds issued to a mortgagee obligee (and the bond in this suit was one for indemnity as well).

It is elemental that a party breaking a contract is liable for all losses which are natural, certain and proximate.

In *Trainor Co.* v. *Aetna Casualty Co., supra,* Mr. Justice SUTHERLAND stated the primary or general rule applicable to mortgagee obligees in a bond guaranteeing completion, as follows:

> "Petitioner is entitled to be put in as good position in respect of its debt as it would have occupied if the buildings had been completed in accordance with the terms of the undertaking; * * *"

In *Kidd* v. *McCormick, supra,* the New York Court of Appeals stated the primary or general rule as follows:

> "Stated in its broadest form, the plaintiff is to have that compensation, which will leave him as well off as he would have been had the contract been fully performed."

Applying to this case the rules so laid down, it needs no argument to show that Prudence Company in this case cannot be put in as good position and cannot be as well off unless interest, taxes and insurance premiums are included in its damages.

If the building had been completed and ready for occupancy with all equipment installed, on December 16, 1930, Prudence Company could have immediately rented it instead of having to wait until October 1, 1931; and out of such rent it would have had a source of payment of its interest, taxes and insurance premiums.

The words "in respect of its debt" contained in the opinion of Mr. Justice SUTHERLAND, in *Trainor* v. *Aetna*, just quoted, have, as we read the opinion, a special significance in a case of this kind, and clearly mean that Prudence Company is to be put in as good position in respect of the interest on its investment and the taxes and insurance premiums which it must pay to protect its investment as it would have been in had the building been completed as guaranteed. Moreover, the words just quoted indicate, as we read them, that there is a direct causal connection between failure to erect the building and the failure of Prudence Company to obtain a source of interest on its debt.

Certainly, Prudence Company's loss of interest on its debt and the taxes and insurance premiums with respect thereto are directly related to the surety bond. If default under the bond were not an accompaniment of default in

completion within the anticipation of the parties, there would be no purpose in a mortgagee obtaining a bond for completion of a building. The fact that a breach of the obligation to pay the mortgage is also involved does not alter the causal relation between the delay in completion of the building and the loss of interest, taxes and insurance premiums.

Cf. Sauter v. *New York Central & H. R. R. Co.*, 66 N. Y. 50;
Lane v. *Atlantic Works*, 111 Mass. 136;
Torts Restatement (Am. L. Inst.) §447;
See *Purchase* v. *Seelye*, 231 Mass. 434.

Especially is this so where, as in this case, resort was to be had to the building guaranteed by the surety bond only in case of a default in the payment of the mortgage loan.

This causal relation is emphasized by the ground lease cases, where the bond guarantees the erection of a building by the lessee on leased property, and the Courts hold that damages are measured not simply by the addition which the building would make to the value of the reversion, but by the rent which its erection would secure. Thus in *O'Brien* v. *Illinois Surety Co.*, 203 Fed. 436, 439, C. C. A. 6, the Court (Judge Denison) stated:

> "Whenever a building, to be erected by a lessee, will materially increase the rental value of the premises, and the lease reserves to the lessor such a periodical rent that his stipulated right of reentry into the vacant premises may not be, of itself, ample indemnity for any default, it is clear that the building is intended to constitute, not only an additional rental payable at the end of the term,

> but also an additional security for the rent currently accruing. This intention is not alleged in the petition now under review, but we think the allegation unnecessary. Such intent stands out on the face of every such contract, and only under unusual conditions could it be lacking."

See also:

Rock v. *Monarch Building Co.*, 87 Ohio St. 244;
Kanter v. *New Amsterdam Casualty Co.*, 195 App. Div. 756, 760, aff'd 233 N. Y. 602.

Within the broad general rule of damages above stated, different kinds of testimony and different elements of damage may be considered in order in each case to put the obligee in as good position as he would have been had the bond been performed. Thus, in *Trainor* v. *Aetna*, Mr. Justice SUTHERLAND stated:

> "and this can be done *here* only by giving it the amount of the difference between the value of the unfinished buildings and their value as it would have been if completed in accordance with the agreement—see *Kidd* v. *McCormick, supra,* p. 398—but exceeding neither the *amount due on its debt* nor the amount of the bond.
>
> "It appears from the findings that this difference would be about $26,000, while the amount now due petitioner is $14,973.98, together with interest thereon from August 13, 1928."

The very fact that in *Trainor* v. *Aetna* the mortgagee obligee was given judgment for the amount due on his mortgage, *together with interest,* shows how clear is Prudence Company's right to interest in this case.

In *Kidd* v. *McCormick,* the Court states, immediately after the quotation made at the beginning of this point (*supra,* p. 38):

"* * * With more particularly, he has a right to a house as good as that which the defendants agreed to furnish; and his damages is the difference between the value of the house furnished and the house as it ought to have been furnished. One kind of testimony by which that difference may be made known, is that of experts, saying what would have been the value of the one, and what is the value of the other. Another kind of testimony is that of experts, what it would cost to complete the unfinished house up to the mark of the contract. Another kind is, when the house has been in fact finished, up to that mark, what it did in fact cost to finish it. But these ways all lead to the same end; what is the difference in value between the unfinished house and a house had it been finished as agreed upon. And this is to be observed of the last-named kind of testimony; *first,* that the plaintiff is not under obligation to go on and finish the house; *second,* that he cannot always finish it, as he could not in the case in hand, at the day called for by the contract, when there will come into the *damages* the element spoken of by Marvin, J., in 33 N. Y. (*supra*)* of *loss from delays;* and *third,* that the cost of actual building may have increased after the day of performance, and so be a detrimental gauge of damage for the defaulting contractor" (p. 396).

Whether the rule of damages be considered from the standpoint of difference in value, cost of completion, or impairment of security, the broad primary rule of putting Prudence Company in as good position as it would have been had the building been properly completed and within the time specified requires, under any of such rules, allowance of its actual loss in interest, taxes and insurance premiums.

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* *Morrell* v. *Irving Fire Ins. Co.,* 33 N. Y. 429.

1

The difference in value was one of the rules of damage which the respondents contended in the Circuit Court of Appeals and in their brief in this Court in opposition to the granting of this certiorari (q. v., pp. 8-11) should be the measure of damages in this case.

The Circuit of Appeals referred to the rule of difference in value as applicable in this case, but, erroneously, as we submit, concluded that interest, taxes and insurance premiums are excluded by such rule. From the very nature of surety bonds such as here involved, as well as the unreality of any valuation of an incomplete building, the phrase "difference in value" must be considered an approximate suggestion rather than a hard and fast formula. Specific rules including all the different elements of damage and sufficient to govern all cases cannot be couched in a sentence or a paragraph.

The rule that an obligee is entitled to be put in as good position in respect of its debt as it would have occupied if the buildings had been completed in accordance with the terms of the undertaking, is founded upon too firm a foundation of right and fair dealing to permit whittling away by slavish or blind adherence to a fixed formula.

While the rule of difference in value is not necessarily the sole standard of measuring damage in this case, the fact remains that even if that rule were to be applied in this case interest, taxes and insurance premiums during the period of completion must necessarily enter into the determination of difference in value.

As was stated in *Kidd* v. *McCormick* (see p. 23, *supra*), so here. Lack of a completed building could not have been "supplied * * * by a purchase in the market." An uncompleted building can be said to have value only in terms of its value when completed.

Necessarily, during the period required for completing a building, the owner (having purchased the uncompleted building) must pay, or—and it is the same thing—must lose, interest on his investment, as well as taxes and insurance premiums on the property. Thus, loss of interest on the investment, taxes and insurance premiums are included in the damages for delay which arise from the fact that, as Judge FOLGER stated:

> "he cannot always finish it" (the building) "* * * at the day called for by the contract."

Likewise, if we approach the matter from the standpoint of what a willing buyer would pay and a willing seller would take for the building in its condition on December 16, 1930, there is no escape from the conclusion that a willing buyer would necessarily be required to deduct from any amount which he otherwise would pay for this property on December 16, 1930, (1) interest on his investment (pending completion of the building), plus (2) the cost of labor and materials required in completion "up to the mark of the contract" and also (3) taxes and insurance premiums accruing during completion.

Assuming, then, that some expert should attempt to testify (as respondents insisted in the Court below should have been done) concerning said difference in value between the building in its state as of December 16, 1930 and the building completed as it should have been on that date, the result would be, and can be, no different from

that actually arrived at by the trial Court in this case. If anyone had bought this building in its uncompleted state on December 16, 1930, he must necessarily deduct from the amount he would pay for a completed building:

1. the cost of carrying the building pending its completion,—and that necessarily would include interest on his investment in the property (which in this case is $6,575,000), and such interest must run from the time he bought the property (in this case that date must be December 16, 1930) up to the time the building was completed (in this case October 1, 1931);

2. the cost of taxes and insurance pending completion;

3. the actual amount necessary to pay for labor and materials to complete the building, including whatever charges might be necessary for protection during completion;

and

4. the cost of supplying omissions and the difference in cost between the inferior materials which were substituted and the materials which the plans and specifications called for; this is necessary, because we must assume a building valued as though completed in accordance with the plans and specifications.

The above items and only the above items were included as elements of damage in the judgment in this case.

2

If we start from the point of view of the cost of completion, which the Circuit Court of Appeals stated "will be the guide" (R. p. 884), the first thing that is plain is that the payments for labor (including supervision) and materials do not represent the entire "cost of completion." (*Cf.* FOLGER, *Ch. J.*, quoted at p. 25, *supra.*)

Taxes, insurance premiums, and interest on the invesment during the construction period are uniformly treated for accounting, rate-making and general legal purposes, as part of the cost of construction, and must be included in "the entire cost of the erection, construction and completion of said building" (R. p. 596), which the sureties agreed to pay.

Thus, it is stated in *Horwath & Toth, Hotel Accounting* (1928), at page 284:

> "The cost of a new hotel includes the contract price as adjusted by extras and allowances resulting from changes in plans and in specifications, architect's fees, *interest on borrowed money and real estate taxes during construction* and such incidental expenses as permits, licenses, *and insurance.*"

See also:

Ohio Utilities Co. v. *Commission,* 267 U. S. 359, 361-63;

Denver Union Stockyard v. *United States,* 57 F. (2d) 735, 741-42 (D. Colo.);

Palmolive Co. v. *Conway,* 56 F. (2d) 83, 86 (C. C. A. 7);
United States v. *New York,* 160 U. S. 598, 621;
2 Kester, Accounting Theory and Practice (2d Ed.) 325-26.

It is significant in this connection that the building loan agreement provided for payment of interest out of the periodic advances during construction by the Principal (R. p. 576); and the bond provided, in case of completion by the Surety, for payment to Prudence Company out of unadvanced moneys, of interest as it accrued, on the entire amount theretofore advanced (R. p. 599).

The interest charge on such a completion job necessarily includes interest on the entire amount already invested in the building; it would be part of the owner's cost of construction, as just pointed out; and it is equally part of the lender's cost of completion.

3

The result is the same, if we apply the principle contained in the statement of the Circuit Court of Appeals that (R. p. 881):

> "The true measure of damages to this appellee, is the extent to which its security was impaired by the failure to complete in accordance with the plans and specifications."

That which was secured was petitioner's investment ($6,575,000) with interest thereon.

As Lord Justice Romer stated in *In re Atkinson,* L. R. [1904] 2 Ch. D. 160:

> "the security is a security, not only for principal, but for interest."

The "security" was to have been the building.

> "fully completed and ready for occupancy as a modern hotel not later than the 16th day of December, 1930, together with all equipment customary in a building of the type provided for in said building loan agreement, installed not later than the 16th day of December, 1930."

Any inquiry, therefore, concerning "the extent to which its security was impaired by the failure to complete" must necessarily embrace and envisage what petitioner lost because the building was incomplete and not ready for occupancy as a modern hotel, with all equipment installed; and this necessarily leads to the inevitable finding that petitioner has lost an income from the building out of which it could pay interest on its investment, taxes and insurance. Thus one of the elements of impairment of petitioner's security is the loss of income from the building to the extent necessary to pay interest, taxes and insurance.

POINT III

The provisions of the surety bond in this case specifically obligated the surety in express terms to pay interest on the loan, and taxes and insurance on the mortgaged property, until the date of actual completion of the building in accordance with the plans and specifications.

The statement of the Circuit Court of Appeals (R. p. 884) that

> "there is no condition, express or implied, respecting payment of the principal or the interest of the loan, taxes or insurance"

entirely disregards the provisions of the bond in this case.

It is not necessary or customary to set forth in a contract, which is primarily concerned with obligations of *performance,* all the possible items of damage in case of its breach. But the bond in this suit is more than usually all-inclusive in its terms, and its language adds a further specific ground for upholding interest, taxes and insurance as part of the contemplated damages.

1. *As to interest*:

Included in the obligations of the defendants contained in the surety bond is the following:

> "• • • and shall *make good* any and every other *default by the Principal in performing* any of the other terms, *covenants* or conditions in said *building loan agreement* set forth by the Principal to be kept and performed *up to and including the completion of and payment for said building* and installation of and payment for said equipment • • •" (R. pp. 596-97).

The building loan agreement and all and singular the terms thereof, are made a part of the surety bond (R. pp. 592-93) and in such surety bond the defendants state that they "are thoroughly familiar with all of the terms, provisions, conditions and requirements contained in said building loan agreement" (R. p. 595).

Turning then to the covenants of the Principal set forth in that building loan agreement, we find the following (R. p. 568):

> "and the Borrower" (Principal, Central Park Properties, Inc.) "agrees * * * to perform and comply with all and every of the covenants, terms and conditions herein and *in said bond and mortgage contained,*"

and the building loan agreement further specified that (R. p. 568)

> "Said loan shall be evidenced and secured by the bond of the Borrower"

and also (R. p. 569):

> "Third: Said bond shall be conditioned for the repayment of the amounts advanced thereon on the 16th day of December, 1930; together with interest at the rate of six (6%) per centum per annum due and payable on the 16th day of December, 1930, and quarter-annually thereafter and as hereinafter provided."

The building loan agreement further provides that interest on the full principal amount shall run from the date fixed for completion, whether or not the building be completed on that day (R. p. 570).

It follows, therefore, that when the defendants in their surety bond undertook to make good any default by the Principal

> "in performing any of the * * * covenants * * * in said building loan agreement set forth by the Principal to be kept and performed *up to and including the completion of* * * * said building and installation of * * * said equipment"

the defendants assumed an express contract obligation to pay the interest which the trial Court has awarded, viz., interest on the principal of the loan from December 16,

1930 to October 1, 1931, the date of the "completion of the building."

Thus it results that, apart from other evidence of what damages were contemplated, the respondents in their surety bond assumed a definite contract obligation to pay the interest which the trial Court awarded.

Citations by the Circuit Court of Appeals to the effect that "in the absence of express contract to pay interest, interest as damages cannot be recovered apart from the principal of the debt," have no application to the present case because, (1) as just shown above, there was here an express contract to guarantee interest up to and including the completion of and payment for said building; (2) the rule cited by the Circuit Court of Appeals has no application to a suit such as this is, where interest on a separate but related contract or sum of money is part of the *principal* of the damages (see citations, *supra,* pp. 33-35); and (3) loss of interest was part of the damages within the contemplation of the parties.

The sureties argued below that the liability for interest was in some way qualified by Mr. Lefcourt's separate and personal guaranty (Exhibit 10—R. p. 678—), which specifically guaranteed both the completion of the building and "the punctual payment of the full principal sum and interest of the bond and mortgage above described and all amounts advanced and to be advanced thereon and of any extension agreement thereof" (R. p. 680).

The fact that a collateral bond guaranteeing payment of the full amount of the mortgage makes specific mention of the interest on the mortgage along with the principal has nothing to do with the sureties' liability on an entirely separate bond which guarantees completion at a fixed time, and indemnity against default or delay in completion.

Moreover, Mr. Lefcourt's guaranty was limited (R. pp. 571, 681) by provisions typed into the printed form, so as to terminate upon the issuance of a certificate of occupancy (Exhibit 39), which certificate "was not a certificate of completion" (R. pp. 494, 879), and did not imply that the building complied with the plans and specifications (R. p. 494). In other words, Mr. Lefcourt's guaranty became "null and void" before the time when respondents could be called upon to make good under their bond.

Clearly, nothing in Mr. Lefcourt's guaranty or in any inference to be drawn from it, detracts from the clear language of the surety bond in this case or from the force of the reasoning and decisions which establish that interest, taxes and insurance during completion are part of the damages resulting from delay in completion.

The indemnity provisions of the surety bond, already discussed, (*supra*, pp. 27-28)—and Mr. Lefcourt's guaranty contained no indemnity provisions—also specifically obligate the sureties to the payment of interest lost during the period of completion.

At the risk of repetition, we again ask, how can there be indemnity if the petitioner is not placed in just as good a position as if the building had been completed on December 16, 1930?

2. *As to insurance*: The building loan agreement which the sureties guaranteed requires the Principal to pay (R. pp. 580-81):

> "fire, lightning and steam boiler explosion insurance together with any other insurance deemed necessary by Lender" (petitioner).

3. *As to taxes*: The surety bond itself recites that the bond is to guarantee completion of the building on December 16, 1930, in strict accordance with the building loan agreement and plans and specifications, and also "free from all liens."

Also among the obligations of the Principal as set forth in the building loan agreement was the obligation that petitioner's mortgage was to be "a valid first lien upon the premises" "free and clear of all liens and encumbrances" (R. p. 568).

Certainly the above obligations were violated by the non-payment of taxes. How can a mortgage be a first lien, as respondents guaranteed this to be, unless taxes on the mortgaged property are paid? (*Cf.* N. Y. Real Prop. Laws §253 [3].)

Moreover, payment of taxes is also covered by the provisions of the building loan agreement (R. p. 576) giving petitioner, as Lender, the right to apply any part of any advance in payment of interest or taxes due and declaring that the amounts so applied shall be deemed advanced to Central Park Properties, Inc. Those provisions clearly show the Principal was obligated to pay these items.

The building loan agreement certainly contemplated a building which when completed was to be free and clear of taxes and which was to be covered by proper insurance pending completion.

We believe it is obvious, moreover, that taxes and insurance premiums,—actual out-of-pocket payments,—were necessary expenditures for the completion of the building; otherwise in the case of fire or sale for unpaid taxes, petitioner would have had no building even after having spent large sums to complete it.

POINT IV

The measure of damages adopted by the trial Court was supported by proper evidence and conformed with all legal requirements.

The three classes of damage included in the judgment are set forth in the statement of the verdict directed (pp. 10-12, *supra*).

Respondents have repeatedly claimed that petitioner failed in its proof of damages in that it offered no *opinion evidence* of the difference between the value as an entirety of the property with the building uncompleted on December 16, 1930, and the value the property would have had if the building had been completed on that date according to the plans and specifications.

Inasmuch as this question may arise again, we respectfully submit that there is nothing in *Trainor Co.* v. *Aetna Casualty Co.* or in *Kidd* v. *McCormick* or in any other case which requires any different kind of proof than petitioner furnished. On the contrary, the petitioner's case on the amount of damages is in accordance with those two cases.

Respondent's liability to petitioner arises from the terms and provisions of the surety bond to which, and to the fullness of the scope contemplated thereby, we have already called attention.

In *Kidd* v. *McCormick* the Court of Appeals pointed out that the differences discussed were chiefly in

> "the *kind of testimony* by which the amount of damages was to be got at, rather than the *rule* that was to govern" (83 N. Y. at p. 397).

The Court then described three kinds of testimony, which the Circuit Court of Appeals in its opinion (R. p. 881) here also referred to, namely:

1. testimony of experts as to what would have been the value of the completed house and what is the value of the uncompleted house;

2. testimony of experts, "what it would cost to complete the unfinished house up to the mark of the contract"; (here also, as the Court stated, "the plaintiff is under no obligation to go on and finish the house." See also, surety bond—R. pp. 602-03); and

3. testimony as to the actual cost of finishing.

There is no necessity of furnishing every kind of testimony. The testimony offered by Prudence Company meets all the variations of the rules stated above.

1. We have already shown (*supra*, pp. 42-44) that interest, taxes and insurance must enter into any estimate of comparative value of the uncompleted and the finished building.

2. In proof of the damage suffered by omissions and substitutions which Prudence Company did not correct, testimony of experts as to the cost of completion was introduced. Prudence Company proved the reasonable cost of supplying the omissions and the reasonable difference in cost between the materials which had been substituted and the materials which the plans and specifications called for.

The findings of the trial Court with reference to the reasonable value of omissions and inferior substitutions

have in nowise been questioned by the Circuit Court of Appeals.

3. With respect to the work which was done in completion Prudence Company showed actual cost of labor and materials incorporated in the building.

Prudence Company did actually finish the building and therefore, under *Kidd* v. *McCormick* as well as under the elemental principles of damages, petitioner is entitled to the amount expended in order to do what the defendants did not do.

As stated by Mr. Justice CARDOZO in *Comey* v. *United Surety Co.*, 217 N. Y. 268, 276:

> "* * * The fact that he did complete it makes the proof of his damages more certain."

4. The Court of Appeals in *Kidd* v. *McCormick* also recognized damages for delay as an independent element, stating that

> "this is to be observed of the last-named kind of testimony" (testimony as to actual expenditures in completion) * * * "that he cannot always finish it * * * at the date called for by the contract, when there will come into the damages the element * * * of loss from delays" (83 N. Y. at p. 397).

The loss from delays cannot be better measured than by the interest lost and taxes and insurance premiums paid during the period of delay.

We respectfully submit, therefore, that every requirement has been met whereby this Court may rule that the three items of damage included in the judgment, namely,

1. Interest,

2. Actual cost of completion (including taxes and insurance),

and

3. Reasonable value of omissions and inferior substitutions,

were properly included in the judgment.

Conclusion

Upon adjudication by this Court that the three items of damage above mentioned are recoverable, a direction for reinstatement of the judgment of the trial Court would follow as a matter of course but for the direction for a new trial contained in the decree of the Circuit Court of Appeals.

A new trial has been ordered by the Circuit Court of Appeals on the ground of the exclusion of evidence "tending to show" that the president of the petitioner consented to certain substitutions, "*if* the appellee's" (petitioner's) "president had authority to waive the requirement of a written waiver or consent" (R. pp. 882-3). The evidence so excluded (R. p. 213) related to a supposed conversation between the president of the petitioner and a man who had been discharged from the work and who, at the time of the alleged conversation, had no legal relationship to it (see footnote, pp. 13-14, *supra*).

The parties to this action stipulated (R. p. 65) that the same be tried before a jury of one and that both parties should be deemed at the conclusion of the trial to

have moved for direction of verdict "without reservation of any right to have any issue or issues submitted to the jury."

There is, therefore, no constitutional restriction on the power of this Court, in reviewing such a verdict, to direct whatever disposition may be determined proper, including a modification in respect of part only of the judgment.

United States v. *Salmon,* 42 F. (2d) 353 (C. C. A. 5);

United States Potash Co. v. *McNutt,* 70 F. (2d) 126, 132 (C. C. A. 10);

Becker Bros. v. *United States,* 7 F. (2d) 3 (C. C. A. 2);

Board of Education v. *Maryland Casualty Co.,* 27 F. (2d) 20, 23 (C. C. A. 3).

The form of the verdict and judgment in this case make it particularly appropriate for the exercise of the now well-recognized power of the Court, if a new trial is ordered, to restrict it to the specific issue in respect of which error is found.

Farra v. *Wheeler,* 145 Fed. 482, 486-489 (C. C. A. 1);

Original Sixteen to One Mine v. *Twenty-one Mining Co.,* 254 Fed. 630, aff'd 265 Fed. 469 (C. C. A. 9);

Thorpe v. *National City Bank,* 274 Fed. 200, 202 (C. C. A. 5);

May Department Stores Co. v. *Bell*, 61 F. (2d) 830, 843 (C. C. A. 8);

See *Gasoline Products Co.* v. *Champlin Refining Co.*, 283 U. S. 494, 498-499;

Cf. Baltimore & Carolina Line v. *Redman*, 295 U. S. 654 (modifying a judgment of reversal by the Circuit Court of Appeals by substituting a direction for dismissal on the merits in place of a direction for a new trial).

Such power is all the clearer and more extensive in a case such as this, where no issues were submitted to a jury.

In view, therefore, of the stipulation (R. p. 65), we respectfully submit that this Court may, in addition to reversing the Circuit Court of Appeals,

(1) Conclude (as we submit is clearly the case) with the whole record before it that there is nothing to prevent the reinstatement of the judgment of the trial Court;

(2) Direct that, if a new trial is to be had on the ground that objections were improperly sustained to questions "tending to show" that an officer of the petitioner consented to certain substitutions, the decree of the Circuit Court of Appeals be modified so as to direct that such new trial be limited to the issue of the effectiveness of any alleged waiver, and the reasonable value of the omissions or substitutions, if any, which were "effectively consented to" (R. p. 884);

or

(3) Remand the case to the Circuit Court of Appeals with leave to petitioner to apply for a rehearing on the question of waiver.

The decree of the Circuit Court of Appeals should be reversed or modified so as to embody a direction that interest on petitioner's investment between the date on which the building should have been completed and the date on which it was actually completed, and also taxes and insurance premiums paid during such period, be included as items of damage, and also that if a new trial is to be had, the issue on new trial be limited to the issue of effectiveness of any alleged waiver and the reasonable value of the omissions or substitutions, if any, which were effectively consented to.

New York, December 21, 1935.

Respectfully submitted,

ALFRED T. DAVISON,
Counsel for Petitioner.

ALFRED T. DAVISON,
MARTIN A. SCHENCK,
ORRIN G. JUDD,
Of Counsel.